

**Letter Report: Some Taxpayers Are Being
Incorrectly Included in the Federal Payment
Levy Program**

September 2001

Reference Number: 2001-40-150

This report has cleared the Treasury Inspector General for Tax Administration disclosure review process and information determined to be restricted from public release has been redacted from this document.



DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

INSPECTOR GENERAL
for TAX
ADMINISTRATION

September 13, 2001

MEMORANDUM FOR COMMISSIONER, SMALL BUSINESS/SELF-EMPLOYED
DIVISION
COMMISSIONER, WAGE AND INVESTMENT DIVISION

Gordon C. Milbourn

FROM: (for) Pamela J. Gardiner
Deputy Inspector General for Audit

SUBJECT: Final Letter Report - Some Taxpayers Are Being Incorrectly
Included in the Federal Payment Levy Program

This report presents the results of our review to determine if the Internal Revenue Service (IRS) properly included taxpayers in the Federal Payment Levy Program (FPLP) and properly refunded erroneous levy payments to taxpayers when appropriate.

In summary, we found that while the first phase of the implementation of the FPLP has been mostly successful in assisting taxpayers in paying their taxes owed, opportunities exist for the IRS to enhance the FPLP. The IRS can more effectively ensure that only the correct taxpayers are included in the Program and that sufficient information is available to determine why FPLP payments are reversed.

We recommended the Commissioner, Small Business/Self-Employed (SB/SE) Division, ensure that the computer program designed to exclude deceased taxpayers from the FPLP works as intended. The Commissioner, SB/SE Division, should also coordinate with the Financial Management Service (FMS) and the paying agencies to ensure that a sufficient explanation of why payments are reversed is provided in the taxpayers' accounts and that these explanations are used to identify potential problems with the FPLP that could adversely affect taxpayers.

The IRS took corrective action on recommendation 1. The IRS disagreed with recommendations 2 and 3 because it believed that the information it receives from FMS is sufficient to appropriately reverse payments. Also, the IRS did not believe that the more detailed reversal information from FMS would provide it with any problem solving information. While we still believe our recommendations to the Commissioner, Small Business/Self-Employed Division, that address this issue are valid, we do not intend to

elevate the disagreement to the Treasury Department for resolution. IRS management's comments have been incorporated into the report, where appropriate, and the full text of their comments is included as an appendix. We have also addressed specific points in the report.

Copies of this report are also being sent to the IRS managers who are affected by the report recommendations. Please contact me at (202) 622-6510 if you have questions or M. Susan Boehmer, Acting Assistant Inspector General for Audit (Wage and Investment Income Programs), at (770) 936-4590.

Letter Report: Some Taxpayers Are Being Incorrectly Included in the Federal Payment Levy Program

Objectives and Scope

The objectives were to determine if the IRS properly included taxpayers in the FPLP and properly refunded erroneous levy payments to taxpayers when appropriate.

The objectives were to determine if the Internal Revenue Service (IRS) properly included taxpayers in the Federal Payment Levy Program (FPLP) and properly refunded erroneous levy payments to taxpayers when appropriate. To achieve our objectives, we selected all 73 taxpayers whose payments were reversed¹ (115 reversals) from the 5,354 taxpayers with FPLP payments made between July 2000 and March 2001. We obtained and reviewed IRS and Financial Management Service (FMS) account information for these taxpayers and held discussions with IRS and FMS personnel to determine if these taxpayers should be included in the FPLP, why the payments were reversed, and whether the reversed payments were refunded to taxpayers when appropriate.

We conducted the review in the National Headquarters and the Atlanta Area Office between December 2000 and May 2001. This audit was performed in accordance with *Government Auditing Standards*.

Major contributors to this report are listed in Appendix I. Appendix II contains the Report Distribution List.

Background

The Taxpayer Relief Act of 1997 authorized the IRS to levy up to 15 percent of certain federal payments owed to taxpayers.

To help the IRS collect taxes owed, the Congress passed the Taxpayer Relief Act of 1997,² authorizing the IRS to work directly with other government agencies to take up to 15 percent of certain federal payments owed to taxpayers. This taking of money is commonly referred to as a “levy.” The IRS implemented the FPLP to collect part of these payments.

¹ These taxpayers were given credit for the FPLP payments but the payments were subsequently returned to the Financial Management Service.

²Pub. L. No. 105-34, 111 Stat. 788.

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The FPLP is an automated process between the IRS and the FMS, in which the IRS will levy up to 15 percent of certain federal payments made by the FMS to delinquent taxpayers. The levy will continue until the liability is paid in full or the account is otherwise resolved, such as through the establishment of a monthly payment agreement.

The first phase of the FPLP, which began in July 2000, included levies on payments to retired federal employees and payments to vendors with federal contracts. During the first phase of the FPLP implementation, the IRS has been successful in collecting millions of dollars in taxes owed. See the chart below.

Total Dollars Collected Through the FPLP

Type of Taxpayers	Number of Taxpayers	Dollars Collected (Rounded)
Individuals	4,705	\$1.6 M
Businesses	649	\$6.0 M
Totals	5,354	\$7.6 M

Source: Payment Transaction File obtained from the IRS. Data is from July 2000 through March 13, 2001.³

During the second phase, which was scheduled to begin in April 2001, the IRS and FMS plan to add payments made to federal employees for travel advances and reimbursements, salaries, and payments made to Social Security Administration (SSA) recipients to the FPLP. The General Accounting Office (GAO) estimated that there are approximately 232,000 SSA recipients who owe taxes.

³ We did not validate the reliability of the data in the Payment Transaction File.

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Results

While the first phase has been mostly successful in assisting taxpayers in paying their taxes owed, opportunities exist for the IRS to enhance the FPLP in the following areas:

- The IRS incorrectly included some taxpayers in the FPLP.
- The IRS did not have sufficient information to determine why FPLP payments were reversed.

We did not identify any erroneous payments that should have been refunded to taxpayers.

The Internal Revenue Service Incorrectly Included Some Taxpayers in the Federal Payment Levy Program

Some taxpayers are being incorrectly included in the FPLP.

Some taxpayers are being incorrectly included in the FPLP. Our review of information for all 73 taxpayers' accounts where the IRS reversed the payments received showed that 35 (48 percent) taxpayers were deceased. The IRS had incorrectly received FPLP payments totaling \$7,945 for these taxpayers.

In the remaining 38 cases, we did not identify any information in the taxpayers' accounts that indicated whether they should or should not be included in the FPLP.

IRS procedures require that prior to including any taxpayer in the FPLP, the IRS should verify whether the taxpayer is deceased. If deceased, the taxpayer should be excluded from the FPLP. If the taxpayer dies after being selected for the FPLP, the IRS should remove the account from the FPLP.

IRS management did not ensure that the FPLP computer program correctly identified deceased taxpayers. The program did not check all tax years for deceased

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taxpayer information. As a result, there were cases in which the deceased taxpayer information was in one tax year but not in all tax years for the taxpayer.

IRS management took positive actions when it recognized that some deceased taxpayers were being included in the FPLP and implemented a computer programming change in January 2001. This change allowed the IRS to use SSA death information to identify deceased taxpayers. However, the revision did not recognize the “00” in the year 2000 as a legitimate number. While the program identified taxpayers that died before or after the year 2000, it did not identify taxpayers that died in the year 2000. We determined that 27 of the 35 taxpayers died in the year 2000. IRS management was not aware of this year 2000 problem until we brought it to their attention.

In October 2001, the IRS plans to add payments made to approximately 232,000 SSA recipients to the FPLP. Many of these taxpayers are elderly and could be affected by this problem.

Burden on the surviving family members of the deceased taxpayers and negative publicity for the IRS could result by incorrectly including deceased taxpayers in the FPLP. Incorrectly including taxpayers in the FPLP could also distort management reports that are used to provide information to the Congress. While we determined that all payments had been correctly reversed in the cases we reviewed, our analysis showed there are still 22 deceased taxpayers included in the FPLP that should be removed to prevent their payments from being incorrectly sent to the IRS.

Recommendation

1. The Commissioner, Small Business/Self-Employed (SB/SE) Division, should ensure that the computer program designed to exclude deceased taxpayers from the FPLP works as intended.

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Management's Response: The IRS made programming corrections to properly recognize deceased taxpayers and remove them from the FPLP on April 13, 2001.

The Internal Revenue Service Did Not Have Sufficient Information to Determine Why Federal Payment Levy Program Payments Were Reversed

The IRS did not have sufficient information to determine why payments for 38 taxpayers, totaling \$38,153, were reversed.

For the period July 2000 through March 2001, there were 115 FPLP payments totaling \$46,099 that were reversed from 73 taxpayers' accounts. Neither the IRS nor FMS personnel had sufficient information to determine why payments for 38 of the 73 taxpayers, totaling \$38,153, were reversed. Our auditors were told that they would have to contact the agency that paid the taxpayer to determine why the payment was reversed.

GAO standards require that all transactions and other significant events should be clearly documented (in paper or electronic form) and the documentation should be readily available for examination.

The interagency agreement signed by the IRS and the FMS for the FPLP does not require the FMS to provide or maintain documentation on why payments are reversed. The IRS believed it did not need to know why payments were reversed and, therefore, did not develop procedures.

As previously mentioned, the IRS periodically provides information for the FPLP to the Congress. Without adequate documentation, the IRS cannot explain to the Congress specifically why the FPLP payments for the 38 taxpayers were reversed. Also, the IRS cannot determine if the reversals were made in error, which could impact the taxpayers' account balances. For example, in 2 of the 38 cases, the payments fully paid the balance owed but were later reversed.

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Recommendations

2. The Commissioner, SB/SE Division, should coordinate with the FMS and the paying agencies to ensure that a sufficient explanation of why a payment is reversed is provided in the taxpayer's account.

Management's Response: The IRS disagreed with this recommendation and stated the information it receives from the FMS is sufficient to appropriately reverse the payment. The IRS agreed that some of its field employees may not be sufficiently familiar with the computer coding to provide a full explanation to taxpayers that have been levied through the FPLP. As a result, the IRS will emphasize, via a memorandum, what a payment reversal means when a payment has been returned to the FMS due to a non-entitlement claim by the federal payment agency source.

Office of Audit Comment: The General Accounting Office provides in its *Standards for Internal Control in the Federal Government* that "all transactions...need to be clearly documented, and the documentation should be readily available for examination. The documentation should appear in management directives...and may be in paper or electronic form. In addition, all documentation should be properly maintained." The IRS' management directive (interagency agreement) with the FMS does not include a requirement to maintain documentation on why payments were reversed.

3. The Commissioner, SB/SE Division, should use these explanations to identify potential problems with the FPLP that could adversely affect taxpayers.

Management's Response: The IRS disagreed with this recommendation and stated that it does not believe that reversal information will provide it with the problem solving information indicated. When a payment agency source informs the FPLP that the taxpayer was not entitled to the federal payment, it does not mean potential problems will exist in the FPLP that would adversely affect taxpayers.

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Office of Audit Comment: The IRS accepts FMS' actions to reverse payments from taxpayer accounts without knowing the reasons for those reversals. We believe the IRS can improve its administration of the Program by receiving the reasons for the reversal in order to analyze program trends. For example, if a check is returned to FMS undelivered because taxpayers change of address, FMS will reverse the levy payment until a better address is found. If the IRS knew that the levy payment was reversed due to an old address, it could research its records for an updated taxpayer address and share this information with both the FMS and the paying agency source.

Conclusion

While the first phase has been mostly successful in assisting taxpayers in paying their taxes owed, opportunities exist for the IRS to enhance the FPLP. In October 2001, another 232,000 taxpayers are expected to be included in the FPLP. The IRS needs to ensure that taxpayers are correctly included in the Program and that sufficient information is available to determine why tax payments are reversed to avoid potential negative publicity and questions from the Congress that it may not be able to answer.

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Appendix I

Major Contributors to This Report

Walter E. Arrison, Assistant Inspector General for Audit (Wage and Investment Income Programs)

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Deborah Glover, Audit Manager

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Appendix II

Report Distribution List

Commissioner N:C
Chief Information Officer IS
Chief Counsel CC
National Taxpayer Advocate TA
Office of Management Controls N:CFO:F:M
Director, Legislative Affairs CL:LA
Director, Office of Program Evaluation and Risk Analysis N:ADC:R:O
Audit Liaison - Senior Program Analyst S:C:CP:I

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Appendix III

Outcome Measures

This appendix presents detailed information on the measurable impact that our recommended corrective actions will have on tax administration. These benefits will be incorporated into our Semiannual Report to the Congress.

Type and Value of Outcome Measure:

- Taxpayer Burden – Actual; 35 deceased taxpayer accounts with payments totaling \$7,945 were incorrectly included in the Federal Payment Levy Program (FPLP) (see page 3).

Methodology Used to Measure the Reported Benefit:

The 35 deceased taxpayers are the actual number of taxpayers that were incorrectly included in the FPLP between July 2000 and March 2001. We identified the 35 deceased taxpayers during our review of all of the 115 payments that were reversed for 73 taxpayers during this period. Also, we used information from the Financial Management Service and Internal Revenue Service (IRS) computer system data, which included Social Security Administration date of death data, to determine why the payments were reversed.

Type and Value of Outcome Measure:

- Revenue Protection– Potential; FPLP payments totaling \$38,153 for 38 taxpayers were reversed and the IRS did not have sufficient information to explain why (see page 5).

Methodology Used to Measure the Reported Benefit:

The FPLP payments totaling \$38,153 for 38 taxpayers are the total amount of the payments that were reversed between July 2000 and March 2001 that did not have sufficient information to explain why the payments were reversed. We identified these payments during our review of all 115 FPLP payments that had been reversed during this period. Also, we used information from the Financial Management Service and IRS computer system data, which included Social Security Administration date of death data, to determine why the payments were reversed.

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Appendix III

Management's Response to the Draft Report



COMMISSIONER
SMALL BUSINESS/SELF-EMPLOYED DIVISION

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

AUG 29 2001

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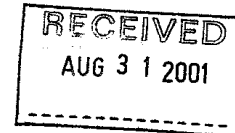
MEMORANDUM FOR DEPUTY INSPECTOR GENERAL FOR AUDIT

FROM:

for Joseph G. Kehoe
Commissioner, Small Business/Self-Employed

SUBJECT:

Draft Letter Report – Some Taxpayers Are Being
Incorrectly Included in the Federal Payment Levy
Program



I appreciate the opportunity to review and comment on the subject draft audit report. I agree with your overall findings that we incorrectly included some deceased taxpayers in the Federal Levy Payment Program (FPLP). This has been corrected.

We implemented the FPLP in July 2000 with the Department of the Treasury and Financial Management Service (FMS). We designed the program to ensure we only included intended taxpayers in the levies issued. Accordingly, the program should have recognized and removed any deceased taxpayer. The programming aspects to remove deceased taxpayers from the FPLP did not work as intended. We made programming corrections on April 13, 2001 to properly recognize deceased taxpayers and remove them from the FPLP.

In addition, I would like to comment on several statements in this report as follows:

- Of the 73 taxpayers identified on the FPLP payment reversal report, 35 were deceased taxpayers. These 35 taxpayers represent 48 percent of the cases reviewed, however they represent less than one percent of the total number of cases on which there were levies.
- Footnote 3 under "Background" reads, "We did not validate the reliability of the data in the Payment Transaction File." While the report concludes the IRS has been successful in collecting millions of dollars in taxes owed, the phrase "the reliability of the data" suggests the data is incorrect and should not be used. We suggest the following change to Footnote 3: "We did not validate the data in the Payment Transaction File." This would eliminate any confusion.

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- Under "The Internal Revenue Service Did Not Have Sufficient Information to Determine Why Federal Payment Levy Program Payments Were Reversed," we disagree with the findings. The IRS receives two types of reversal codes from FMS. Both sets of codes are hidden in the programming and are not available for display on taxpayer records. While the specific reversal codes we receive from FMS do not display on the taxpayer's record, the reversal of the payment does display using a special transaction code that indicates that we received an approved reversal from FMS. We believe this does provide sufficient information to determine why FPLP payments are reversed.

Our comments on the recommendations are as follows:

IDENTITY OF RECOMMENDATION 1

The Commissioner, Small Business/Self Employed (SB/SE) Division, should ensure that the computer program designed to exclude deceased taxpayers from the FPLP works as intended.

ASSESSMENT OF CAUSE

The program to exclude deceased taxpayers from the FPLP did not work as designed.

CORRECTIVE ACTION

We took action to correct this problem when we became aware the program was not working properly. We made programming corrections to properly recognize deceased taxpayers and remove them from the FPLP on April 13, 2001.

IMPLEMENTATION DATE

Completed April 13, 2001

RESPONSIBLE OFFICIAL

Commissioner, Small Business/Self-Employed

CORRECTIVE ACTION MONITORING PLAN

N/A

IDENTITY OF RECOMMENDATION 2

The Commissioner, Small Business/Self Employed (SB/SE) Division, should coordinate with the FMS and the paying agencies to ensure that a sufficient explanation of why a payment reversal is provided in the taxpayer's account.

ASSESSMENT OF CAUSE

TIGTA does not consider the information we currently receive a sufficient explanation of why a payment is reversed.

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CORRECTIVE ACTION

We believe the information we receive from FMS is sufficient to appropriately reverse the payment. However, we agree some of our field employees may not be sufficiently familiar with the computer coding to provide a full explanation to taxpayers who have been levied through the FPLP. We will reemphasize, via memorandum, that an IDRS Transaction Code (TC) 672 with a Document Payment Code (DPC) of 18 means that there has been a payment reversal and the payment has been returned to FMS due to a non-entitlement claim by the federal payment agency source.

IMPLEMENTATION DATE

October 1, 2001 – Memorandum will be issued to field employees.

RESPONSIBLE OFFICIAL

Director, Filing and Payment Compliance, Small Business/Self-Employed

CORRECTIVE ACTION MONITORING PLAN

The appropriate functional staff will advise the Director, Filing and Payment Compliance of any delay in issuing the memorandum.

IDENTITY OF RECOMMENDATION 3

The Commissioner, Small Business/Self Employed (SB/SE) Division, should use these explanations to identify potential problems with the FPLP that could adversely affect taxpayers.

ASSESSMENT OF CAUSE

TIGTA believes more detailed reversal information will help the IRS identify potential problems with the FPLP.

CORRECTIVE ACTION:

We do not believe that the reversal information will provide the IRS with the problem solving information indicated. When a payment agency source informs the FPLP that the taxpayer was not entitled to the federal payment, it does not mean potential problems will exist in the FPLP that would adversely affect taxpayers. However, we will consider any additional information your office can provide that may identify potential problems you believe will adversely affect taxpayers with the reversals.

IMPLEMENTATION DATE

N/A

RESPONSIBLE OFFICIAL

N/A

CORRECTIVE ACTION MONITORING PLAN

N/A

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Please call Martha Sullivan, Deputy Director, Compliance Policy, Small Business/Self-Employed, at (202) 283-2200 if you have any questions.